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Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, D.C. 20554

In the Matter of Amendment of Parts 32 and 64 of the Commission's Rules to Account for Transactions between Carriers and Their Nonregulated Affiliates	)	CC Docket No. 93-251

COMMENTS OF THE
NATIONAL TELEPHONE COOPERATIVE ASSOCIATION

The National Telephone Cooperative Association ("NTCA") submits these comments in response to the Notice of Proposed Rulemaking, FCC 93-453, released by the Commission on October 20, 1993, in the proceeding captioned above ("NPRM"). The Commission is proposing to reevaluate and amend the accounting requirements associated with transactions between regulated carriers and their nonregulated affiliates.[1] NTCA is a national association of approximately 500 small and rural local exchange carriers ("LECs") providing telecommunications services to interexchange carriers and subscribers throughout rural America.

I. THE AMENDMENTS, IF ADOPTED, SHOULD ONLY APPLY TO TIER 1 CARRIERS.

The Commission states that it has now had six years of experience with the joint cost accounting rules.[2] The proposals are apparent fine-tuning efforts that are the result of the Commission's analysis of the operation of those rules over the

[1] NPRM at para. 1. NTCA will refer to these rules as the joint cost accounting rules.

[2] NPRM at para. 9.

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last six years. The NPRM cites numerous individual LEC proceedings that have contributed to the Commission's and staff's analysis and tentative conclusions supporting the need for the possible modifications.[3]

This analysis is exclusively based on activities and attributes of Tier 1 carriers.[4] Only Tier 1 carriers file detailed cost manuals identifying each affiliate and the frequency and specifics of the affected transactions.[5] The inescapable conclusion is that many, if not all, of the proposed accounting amendments contained in the NPRM are designed to deal with the complicated interrelationships between Tier 1 LECs and their nonregulated affiliates. Similarly, the proposals are designed to respond to individual Tier 1 LEC circumstances identified by Commission analysis of these LECs' operations and their cost allocation manuals.[6]

Some of the proposals contained in the NPRM are so confined to the experience of and application to the larger LECs that they will be inapplicable to small and rural LECs. Some of the other specific amendments, however, would impose more complex and

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[3] See, e.g., NPRM at footnotes 11, 36, 38, 39, 49, 58, 67, 108, and 109.

[4] Tier 1 carriers according to the application of the joint cost accounting rules are LECs with annual revenues of $100 million or more.

[5] NPRM at para. 7.

[6] The NPRM also includes tentative conclusions with regard to the joint cost rules as applied to price cap LECs. NPRM at paras. 31, 68-69, and 103.

burdensome requirements than the current rules. In any event, changing existing accounting systems to accommodate such minor changes would be burdensome. This proposed fine tuning is based either on conclusions regarding large LEC's operations or the dynamics of price caps, or both. As such, while those small and rural LECs subject to the joint cost accounting rules have and will continue to comply with the current rules, it is unnecessary and inappropriate to extend these further complications to any other LECs other than the ones for which the experience has led to the proposals. Therefore, should the amendments be adopted, they should only apply to the Tier 1 carriers.

II. SOME OF THE TENTATIVE CONCLUSIONS UNDERLYING THE PROPOSED AMENDMENTS DO NOT APPRECIATE THE NEEDS OF AND POTENTIAL BENEFITS TO RURAL AREAS.

The apparent rationale for the joint cost accounting rules is that public policy dictates that ratepayers of regulated services should and must be protected from cross-subsidizing customers of nonregulated services, and that left to their own devices, LECs will always favor nonregulated customers to the detriment of the public interest. This rationale is based on somewhat tentative theoretical conclusions. These theoretical conclusions are addressed by the joint cost accounting requirements that, in effect, produce the same effect in the opposite direction; i.e., ratepayers of regulated services receive the maximum benefit of the joint cost accounting to the detriment of and potential discrimination of the customers of nonregulated services. As the telecommunications/information-age industry moves towards an ever increasing diversity of services and providers, a system that imposes the maximum benefit for the users of services that remain regulated to the detriment of the users of services that are not regulated will produce the same potential public interest harm, in the opposite direction, as the potential ills the joint cost rules are ostensibly designed to prevent.

The tentative conclusions are even more problematic when applied to small and rural LECs and the customers they serve. First, the administrative cost of adopting and applying the joint cost rules disadvantages small and rural LECs to the point of threatening decisions to make nonregulated services available in the first place, adds to the overall cost and increases the risk of operations. In rural areas, the end users of regulated services are most often the same customers for nonregulated services. In this sense, these complicated rules are designed partly to needlessly protect the right hand from the left.

But most importantly, small and rural telcos are challenged by relatively high costs of low-volume areas resulting in a lack of economy of scale and scope. There is a net benefit to all customers whenever an otherwise solely regulated services provider is able to improve its scale and scope by jointly providing closely related services and facilities for which it can make economical use of its local expertise and presence.

Specifically, in this regard, the NPRM proposes to abandon the fully distributed cost valuation of services for one in which the valuation of services is based on "the higher of fully distributed costs and estimated fair market value when a carrier is the seller, and at the lower of fully distributed costs and estimated fair market value when a carrier is the purchaser."[7] The theoretical basis for wanting to amend the services valuation rules appears to be based on the presumed incentives fostered by price caps or other forms of incentive regulation.[8]

NTCA is concerned by this proposal in that it lacks an appreciation for the needs of rural subscribers and the potential benefits to rural customers of small and rural LECs pursuing nonregulated activities. Where there is a demand for nonregulated services of real value to rural customers, and the local provider of regulated services which is in the best position to use its expertise and local presence decides to provide these services, NTCA submits that in the vast majority of cases, there will be a net benefit to the public. The current regulated services users benefit by a greater economy of scale or scope achieved and a further sharing of costs. The new users of the nonregulated services benefit by having such services available priced at joint cost levels and by further utilizing the expertise of the existing provider.

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[7] NPRM at para. 15. This method only applies if the valuation is not determined by tariff rates or prevailing prices.

[8] NPRM at paras. 31 and 32.

The proposed amendments to the rules for services valuations[9] would appear to impose a requirement that the class of customers who use regulated services should receive a greater, and unfair, benefit of cost sharing (at market rates instead of actual fully distributed costs) for services provided to the nonregulated services entity. This mechanism would seem to impose the same counterproductive results in that it will require cross subsidy from nonregulated service users to regulated service users. The result of such counterproductive measures are to discourage joint service provisions that would otherwise be beneficial to rural subscribers or to impose rules that lead to unfair pricing of nonregulated services compared to regulated services.

The lack of appreciation for rural situations is apparently based in the Commission's view of the world as seen in its price cap experiment and its policy towards cost reduction incentives. As with the application and perceived benefits of price caps, many of these views do not apply to the operations of small and rural telcos. The proposals regarding the valuation of services as contained in the NPRM would be counterproductive to small and rural LEC operations, and therefore the rules do not need to be modified.

III. SOME PROPOSED AMENDMENTS ARE TOO VAGUE FOR COMMENT.

At para. 51 of the NPRM, the Commission proposes that all accounting related to affiliate transactions be subject to

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[9] NPRM at paras. 30-33.

generally accepted accounting principles ("GAAP"). The Commission states that fully subject and connecting carriers would have to use GAAP in determining carrier and nonregulated affiliates' costs. Unfortunately, the one paragraph discussion does not explain what change this requirement would impose. The NPRM does not explain how costs are determined absent GAAP and what the resulting difference in cost would be under a GAAP determination. The discussion does not cite any specific example to explain the need, if any, for the proposed modification. The GAAP amendments should not be adopted until fully described and debated.

IV. USE OF A COMPOSITE RATE OF RETURN WOULD BE UNWORKABLE.

At paras. 66-71 of the NPRM, the Commission discusses possible modifications in the return on investment component of fully distributed costs. One possible change suggested would be for carriers to apply "a composite of the prescribed, interstate rate of return and the intrastate rates of return prescribed or authorized for" a particular LEC.[10] This suggested approach would be unworkable for small telcos, if not for all LECs.

First, a number of states do not regulate small and rural telcos, and therefore, no prescribed intrastate rate of return exists. Even for those that do have regulatory authority over small LECS, the degree of regulation often stops well short of prescribing rates of return. Small LECs should not be forced

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[10] NPRM at para. 71.

into seeking intrastate rates of return solely for interstate joint cost accounting purposes as would be required under the composite approach.

Second, the determination of the proper composite between intrastate and interstate components would impose another burden on LECs and would result in a necessarily arbitrary result. Any decision on the relative measures to base the composite proportions would involve arbitrary determinations inconsistent with the use.[11]

Third, as the NPRM implies, applying a composite rate of return to cost determinations would defer to the states the ability to preempt interstate goals and undermine the Commission's authority over these accounting matters. Such an approach would impose further burdens on carriers and the Commission to examine intrastate methods to determine whether interstate interests are being frustrated.

For these reasons, NTCA supports the continued use of a single, interstate determined rate of return for the purpose of the joint cost rules' application.

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[11] For example, there is no meaning to the jurisdictional nature of a nonregulated affiliate's various operations.

V. CONCLUSION

For the reasons submitted above, the proposed modifications to the joint cost accounting rules should not be adopted for non-Tier 1 LECs. The proposals are based on the analysis and characteristics of larger carriers, do not appreciate the needs of rural subscribers, and are potentially counterproductive if applied to small and rural LECs.

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December 10, 1993

CERTIFICATE OF SERVICE

I, Rita H. Bolden, certify that a copy of the foregoing Comments of the National Telephone Cooperative Association in CC Docket No. 93-251 was served on this 10th day of December 1993, by first-class, U.S. Mail, postage prepaid, to the following persons on the attached list:

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